

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

UNITED STATES OF AMERICA :
 :
 v. : CRIMINAL NO. 98-603-01
 :
ARTHUR TOLL :

GOVERNMENT'S CHANGE OF PLEA MEMORANDUM

I. INTRODUCTION

Defendant Arthur Toll was charged by Superseding Indictment with conspiracy to commit securities fraud and to make false and misleading statements to auditors, in violation of Title 18, United States Code, Section 371 (count 1); securities fraud, in violation of 15 U.S.C. §§ 78j(b), 78ff(a) (count 2); false statements to auditors, in violation of 15 U.S.C. §§78m(b)(2) and (5), 78ff (count 3); mail fraud, in violation of 18 U.S.C. § 1341 (counts 4-7); and wire fraud, in violation of 18 U.S.C. § 1343 (counts 8-12). Defendant was Chief Executive Officer, Chairman of the Board of Directors, and majority stockholder of Regal Communication Corporation ("Regal"), the stock of which was publicly traded over NASDAQ. These charges arise from the defendant's participation in a conspiracy from 1991 until about April 19, 1994, in which the defendant with others, including the Chief Financial Officer, co-defendant Bruce Edmondson, reported millions of dollars of bogus revenue and accounts receivable in Regal's financial statements and also diverted Regal stock worth millions of dollars to themselves and

entities they controlled without paying to Regal the money due. On August 6, 1999, the defendant will enter a guilty plea pursuant to a written plea agreement.

II. TERMS OF THE PLEA AGREEMENT:

The plea agreement is made pursuant to Fed.R.Crim.P. 11(e)(1)(C) and provides for a jointly agreed upon sentence as follows:

- ! 48 months incarceration;
- ! a term of 3 years supervised release;
- ! restitution to be paid as follows:
 - " a certified check in the amount of \$50,000 to be paid at the time of sentencing;
 - " a 100% assignment of the defendant's interest in CMS Private Equity Funds(future benefits of which are currently projected to have a value of approximately \$842,000), which assignment shall be made no later than the time of sentencing;
 - " \$300,000 to be paid at a rate of \$100,000 per year, with payments to commence at the time the defendant is placed on supervised release, and these payments shall be secured by the defendant's stock in First Mortgage Corporation;
- ! a \$10,000 criminal fine to be paid on or before sentencing by certified check, and

! and a special victims/witness assessment in the amount of \$600 to be paid on or before sentencing by certified check.

The specifics of the agreement are set forth in the document itself which is attached as Exhibit A.

III. STATUTES INVOLVED:

A. 18 U.S.C. § 371 (conspiracy -- Count One)

Title 18, United States Code, Section 371 states in relevant part:

If two or more persons conspire to either commit any offense against the United States, or to defraud the United States, or any agency thereof in any manner or for any purpose, and one or more of such persons do any act to effect the object of the conspiracy, each shall be fined under this title, or imprisoned not more than five years, or both.

To establish a violation of 18 U.S.C. § 371, the government must prove the following essential elements:

1. that two or more persons entered an unlawful agreement to commit offenses against the United States, in this case to commit securities fraud and to make false and misleading statements to auditors;
2. that the defendant knowingly and willfully became a member of the conspiracy;
3. that one of the members of the conspiracy committed at least one of the overt acts charged in the indictment; and
4. that the overt act(s) was/were committed to further some objective of the conspiracy.

B. Title 15, United States Code, §§ 78j(b) and 78ff(a); 17
C.F.R § 240.10b-5 (Securities Fraud -- Count Two)

In order to obtain a conviction for securities fraud,
the government must prove the following essential elements beyond
a reasonable doubt:

1. That in connection with the purchase or sale of
any security, the defendant did one or more of the
following:
 - (a) employed a device, scheme, or artifice to
defraud, or
 - (b) made an untrue statement of a material fact
or omitted to state a material fact which
made what was said, under the circumstances
misleading, or
 - (c) engaged in an act, practice, or course of
business which operated or would operate as a
fraud or deceit upon a purchaser or seller,
and
2. that in connection with the purchase or sale of
any security, the defendant knowingly used, or
caused to be used, any means or instruments of
interstate commerce, or of the mails, or of any
facility of any national security exchange; and
3. that the defendants acted willfully, knowingly and
with intent to defraud.

C. Title 15, United States Code, §§ 78m(b) and 78ff(a); 17
C.F.R § 240.13b2-2 (Making False and Misleading
Statements to Auditors -- Count Three)

In order to prove the crime of making false and
misleading statements to auditors, the government must prove the
following essential elements beyond a reasonable doubt:

1. that the defendant was a director or officer of an
issuer;

2. that the defendant, directly or indirectly, did one or more of the following:
 - (a) made or caused to be made a materially false or misleading statement, or
 - (b) omitted to state, or caused another person to omit to state, any material fact necessary in order to make statements made, in the light of the circumstances under which such statements were made, not misleading to an accountant in connection with (1) any audit or examination of the financial statements of the issuer required to be made pursuant to 17 C.F.R. 240, Subpart A or (2) the preparation or filing of any document or report required to be filed with the SEC pursuant to 17 C.F.R. 240, Subpart A, or otherwise; and
3. that the defendant acted willfully, knowingly and with intent to defraud.

The term "issuer" means any company that issues or proposes to issue any security. 15 U.S.C. § 78c(a)(8).

D. 18 U.S.C. § 1341 (Mail Fraud - Counts 4-7)

Mail fraud is prohibited by Federal law which provides in relevant part that:

Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, . . . [and] for the purpose of executing such scheme or artifice or attempting so to do, places in any post office or authorized depository for mail matter, any matter or thing whatever to be sent or delivered by the Postal Service or takes or receives therefrom . . . or knowingly causes to be delivered by mail according to the direction thereon. . . .

shall be guilty of an offense against the United States.

To establish a violation of the mail fraud statute, the government must prove the following essential elements beyond a reasonable doubt:

- (1) that the defendant knowingly devised or intended to devise a scheme or artifice to defraud or to obtain money or property by false or fraudulent pretenses, representations or promises as detailed in the superseding indictment;
- (2) that the defendant did so with the intent to defraud;
- (3) that in advancing or furthering or carrying out his scheme the defendant used the mails or caused the mails to be used; and
- (4) that the misrepresentation or concealment was material.

In general, a false statement is material if it has a natural tendency to influence, or is capable of influencing, the decision of the decision making body to which it was addressed.

E. 18 U.S.C. § 1343 (Wire Fraud - Counts 8-12)

The law of the United States prohibiting wire fraud provides in part as follows:

Whoever, having devised or intending to devise any scheme or artifice to defraud and transmits or causes to be transmitted by means of a wire, radio, or television communication in interstate or foreign commerce, any writings, signs, signals, pictures, or sounds for the purpose of executing such scheme or artifice ...

shall be guilty of an offense against the United States.

In order to sustain its burden of proof for the crime of wire fraud the government must prove the same elements as for

mail fraud, except in advancing or furthering or carrying out his scheme the government must show that the defendant used a wire communication in interstate commerce such as a fax.

IV. MAXIMUM SENTENCE

The Court may impose the following statutory maximum sentence:

- ! Count 1 (conspiracy) -- 5 years imprisonment, 3 years of supervised release, a \$250,000 fine, restitution and a \$50 special victims/witness assessment;
- ! Count 2 (securities fraud) -- 5 years imprisonment, 3 years of supervised release, a \$250,000 fine, restitution and a \$50 special victims/witness assessment;
- ! Count 3 (false statements to auditors) -- 5 years imprisonment, 3 years of supervised release, a \$250,000 fine, restitution and a \$50 special victims/witness assessment;
- ! Counts 4 - 7 (mail fraud) -- 5 years imprisonment, 3 years of supervised release, a \$250,000 fine, restitution and a \$50 special victims/witness assessment;
- ! Counts 8 - 12 (wire fraud) -- 5 years imprisonment, 3 years of supervised release, a

\$250,000 fine, restitution and a \$50 special victims/witness assessment.

Total Maximum Sentence is: sixty years imprisonment, 3 years of supervised release, a \$3 million fine, a \$600 special victims/witness assessment, and full restitution.

V. EVIDENCE IN SUPPORT OF THE ALLEGATIONS:

The government's evidence would prove the following facts, among others, if this case went to trial:

Regal Communications Corporation ("Regal") was a New Jersey corporation located in Fort Washington, Pennsylvania, which engaged in television infomercial marketing through its subsidiary Regal Group, and pay-per-call "900" lines services through its subsidiary Regalfone, Inc. ("Regalfone"). Regalfone's "900" line services included sex talk, psychic and horoscope programs.

Regal's common stock was registered with the United States Securities and Exchange Commission ("SEC") and was traded on the NASDAQ, a national securities exchange, between 1992 and April of 1994. Defendant Arthur Toll, was Regal's Chief Executive Officer, Chairman of the Board of Directors and majority shareholder. Regal and its subsidiaries filed for Chapter 11 bankruptcy protection on September 23, 1994. Regal and its subsidiaries today are defunct entities.

Between 1991 and April 19, 1994, defendant Toll

participated in a conspiracy with co-defendant Bruce Edmondson, Regal's Chief Financial Officer and a Board member, co-defendant Elliot Fisher, Regal's legal counsel, corporate secretary and a Board member, to commit securities fraud and make false and misleading statements to auditors. In addition, he committed, or aided and abetted the commission, of the substantive offense charged in the conspiracy (securities fraud and false statements to auditors), as well as mail and wire fraud. As described more fully below, Toll -- along with Edmondson and Fisher -- falsified and caused others to falsify Regal's financial records and arrange for the publication of false and misleading information concerning Regal's financial condition to the public and Regal's auditors so as to make Regal appear more substantial and profitable than it really was. In addition, Toll -- with Edmondson and Fisher -- diverted Regal stock worth millions of dollars to himself, to Edmondson, and to entities that they controlled without paying to Regal the money due and without disclosing this to Regal's auditors or the public.

**PUBLICATION OF FALSE FINANCIAL INFORMATION: REPORT OF BOGUS
REVENUE AND RECEIVABLES**

I. Fiscal Year 1992

As a result of the defendant's criminal actions described below, Regal's 1992 financial statements were materially false and misleading. In fiscal year 1992, Regal reported retained earnings of \$4.2 million and net income of

\$969,883. The government's expert, a forensic accountant, would testify that in fiscal year 1992 Regal actually had negative retained earnings of \$1.26 million and had a net loss of \$4.5 million.

A. False Regalfone Revenue and Receivables for FY 1992

In fiscal year 1992 defendant Toll, along with co-defendant Bruce Edmondson, manipulated Regalfone's books and records to conceal their diversion of approximately \$500,000 worth of Regal stock for themselves. In addition, they inflated Regalfone's reported revenue and receivables by approximately \$3 million.

1. TEL Free Stock Transaction

Overview: As illustrated in Attachment 1, Toll and Edmondson, with the assistance of Gerald Levinson (a Regal Board member), funneled in April, 1992 over \$500,000 from Regalfone to TEL Entertainment ("TEL") -- a video store owned by Toll, Edmondson and Levinson -- and into their own pockets. Regalfone's books masked the true purpose of the transfer of these funds to TEL by classifying the \$500,000 as "equipment purchase deposits" on Regalfone's books (which had the added benefit of being an asset). Although TEL was owned and controlled by Toll and Edmondson, they created fake invoices to make it appear as if the TEL involved in these transactions was a different company. Thus, they concealed from the auditors the

fact that these transactions were related party transactions. Toll and Edmondson then circulated the money back to Regal to pay for their own Regal stock and warrants.

2. Fake MCI Receivable/TEL Transactions

Overview: As illustrated in Attachments 2 and 3, Toll and Edmondson, again with the with the assistance of Gerald Levinson, inflated Regalfone's reported revenues and receivables by funneling approximately \$760,000 of its own money to TEL (and Gateway) and back to Regalfone in June and July, 1992. Regalfone's books masked the true purpose of the transfer of these funds to TEL by classifying the \$760,000 as "equipment purchase deposits" on Regalfone's books. As was discussed above, Toll and Edmondson created fake invoices to conceal the fact that the TEL involved in these transactions was owned and controlled by them.

When TEL transferred the funds back to Regalfone, notations on the deposit slips -- made either by Toll or his secretary, Berkley Luders, at his direction -- misrepresented that the funds came from "MCI," not TEL. Tom Hodges, a Regal accountant, then booked the money as MCI revenue in Regalfone's general ledger.

3. Fake "Info" Receivable

Overview: As illustrated in Attachment 4, after fiscal 1992 had closed and its auditors were on site, Regalfone booked a

receivable for approximately \$2,252,325, attributable to "Info," which purportedly had been earned July-September, 1992. This reported receivable is bogus because the government's forensic accountant experts have traced the pay down of the receivable to Regalfone's own money which the defendants caused to be secretly circulated through Clark Advertising back to Regalfone.

B. False Regal Group Revenue and Receivables for FY 1992

In addition to their manipulation of Regalfone's books and records, Toll and Edmondson also inflated the revenue and receivables of Regal Group, Regal's infomercial subsidiary, for fiscal year 1992. The two sets of transactions by which they did this are discussed below.

1. Fake Sale of Irons to Uprise Sales, Inc.

Overview: As illustrated on Attachment 5, during fiscal 1992, Regal Group recorded a receivable for approximately \$3.126 million in connection with a purported June 1992 sale of travel irons (called sisson irons) to an entity called Uprise Sales, Inc. ("Uprise"). The receivable, which was on the books as of the end of fiscal 1992, subsequently was paid down during the FY 1992 audit by the deposit of two cashier's checks -- one for \$1.3 million, and the other for \$1.5 million -- that were printed with the name "Uprise Sales, Inc." as the remitter.

This reported receivable is bogus because Regal Group never sold sisson irons to Uprise Sales, Inc. or Uprise, Inc.,

and the money used to purchase the cashier's checks came from Gateway -- Toll and Edmondson's defunct company -- and not Uprise. (Ultimately the money came from Toll and Edmondson's misappropriation of Regal's stock as discussed in section II.B. below.)

2. Fake Inphomation, Inc. Royalty Receivable

Inphomation was acquired by Regal in September of 1993. Prior to this, the companies had a legitimate business relationship in which Regal Group resold to Inphomation media air time which Regal Group had purchased from various cable networks.

At the end of fiscal year 1992, Regal Group's books reflected a \$2,200,232 receivable purportedly due from Inphomation for "royalties" earned July-September of 1992. Carl Wahl, Regal Group's accounting manager, stated that he booked this receivable because Edmondson told him to and presented him with documents confirming the royalty, including a bogus contract signed by Toll and bearing the forged signature of Michael Warren Lasky, the president and owner of Inphomation.

Like the "Info" and Uprise receivables, the Inphomation receivable was fake. Inphomation's owner, Mike Laskey, and controller, Naresh Mirchandani, have confirmed that: (1) Inphomation never owed Regal Group any royalties, let alone one for \$2,200,232; and (2) the documents used by Edmondson to support the receivable are fake.

II. FISCAL YEAR 1993

As a result of the defendant's criminal acts as described below, Regal's fiscal year 1993 financial statements were materially false and misleading.

A. The Clark Circulations

Defendants Toll and Edmondson cooked the books in three different ways in fiscal year 1993, and they all involved Clark Advertising. In fiscal year 1993, Toll and Edmondson used Clark to secretly circulate money back and forth to Regalfone to: (1) pay down the fake \$2,252,325 "Info" receivable booked on Regalfone's books at the end of FY 1992 (as discussed above); (2) fraudulently inflate revenues reported to the public regarding Regalfone's 900 line business (as discussed in this section); and (3) to cover-up the fact that they had received stock from Regal without paying for it (discussed in a Section II B, below).

These transactions had the effect of making Regal appear more financially healthy than it was. More specifically, in fiscal year 1993, Regal reported to its auditors negative retained earnings of \$3.695 million and a net loss of \$7.814 million. The government's expert would testify that Regal's negative retained earnings were actually \$18.7 million and net loss was \$17.4 million.

The bogus revenue booked by the defendants materially misstated Regal's financials for FY 1993.

Overview: Clark Advertising was a private corporation owned by Toll and Edmondson and run by them with the assistance of Joseph Salvati. Clark placed advertising time with TV and radio media to promote Regal's 900 lines. In 1992, Toll and Edmondson came under pressure from the investment community to spin-off the related companies with which Regal did business. To quell these concerns, beginning with its 1992 10K, Regal reported in its public filings that Toll and Edmondson had sold Clark to "an independent group of investors." As discussed below, the evidence shows that this was a lie, and that Toll and Edmondson owned and controlled Clark until the fraud was discovered.

Moreover, Toll and Edmondson also owned and controlled National Audiotex, a service bureau used by Regalfone, which they also failed to disclose in Regal's public filings or to its auditors. Throughout fiscal year 1993, Regal reported that it was owed large receivables by National Audiotex.

As stated above, these lies and omissions had several purposes, one of which was to make it appear as if Regalfone (and ultimately Regal) was earning more revenue than it actually was. Beginning in February 1992, and continuing up until November 30, 1993, the defendants circulated millions of dollars between the checking accounts of Regalfone and Clark. The payments from Regalfone to Clark were treated on Regalfone's books as media

expenses¹, while the payments from Clark back to Regalfone were treated on Regalfone's books as revenue from "National," "Info" (apparently a reference to Inphomation) and "AT&T."

Although Regalfone did purchase some media time through Clark during this period, that amounted to \$5-6 million at most, not the \$24 million claimed in Regal's books. Moreover, all witnesses questioned who are knowledgeable about Clark agreed that there was no legitimate reason for Clark to pay Regalfone over \$24 million during this period, and that Clark never collected money from National Audiotex, Inphomation, AT&T or any other long distance phone company or service bureau which it would need to remit to Regalfone.

B. Diversion of Regal stock

In the spring of 1992, Regal completed a private placement offering of units which allowed Regal to raise over \$4 million from investors. Each unit that was sold consisted of one share of stock and one warrant to purchase stock in the future at a locked-in price.

In the fall of 1992, Toll, Edmondson and Fisher secretly diverted Regal stock worth millions of dollars by having Gateway Telecommunications Corporation ("Gateway")-- a company Toll and Edmondson privately owned and controlled -- exercise

¹ The media expenses were classified as either media placement expenses or prepayment of media.

fictitious warrants purportedly issued in the private placement. Regal was never paid the full amount it was owed for the warrants or for the stock. Defendant Toll then sold 200,00 shares of the resulting stock on the open market and secretly circulated the funds back to Regal -- by way of two cashier's checks -- to pay down part of the bogus Uprise receivable discussed above. See Attachment 4. Defendant Toll personally received an additional 200,000 of these fraudulently issued shares.

* * *

Witnesses and Other Evidence: Had this matter proceeded to trial, the government would have introduced hundreds of documents, charts and graphs, including accounting records, bank records, SEC filings, correspondence, and accountant work papers which would have documented the transactions outlined above. In addition, the government would have called to testify more than 50 witnesses, including experts, to explain these transactions and their impact on the publicly filed documents with the SEC. Accountants would have testified about the misrepresentations made to them during the audits of the publicly traded company. Witnesses identifying the charged mailings and wirings would have also testified. Finally, victims who invested in Regal would have testified, including celebrity Joan Rivers whose companies were purchased in a stock trade transaction and who lost millions of dollars in that deal. Ms. Rivers would have

testified about how she relied on Arthur Toll's representations about the financial health of Regal Communications.

Respectfully submitted,

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Assistant United States Attorney

December 3, 1999

CERTIFICATE OF SERVICE

I hereby certify that on December 3, 1999, I caused to be served by hand deliver and facsimile transmission a copy of the attached government's Change of Plea Memorandum on the defense counsel in this case:

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